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SUBJECT: DRAFT NATIONAL TRADE ESTIMATE REPORT

Ref: STATE 310953

The following is Embassy's input for the National Trade Estimate Report for Turkey:

TRADE SUMMARY

Turkey is a beneficiary of GSP, has Bilateral Investment and Tax Treaties with the United States, and has a customs union with the European Union. (Trade/investment statistics to be provided by Washington agencies).

IMPORT POLICIES

Tariffs and Quantitative Restrictions

As a result of its 1996 customs union with the European Union, Turkey applies the EU's common external customs tariff for third country (including U.S.) imports and imposes no duty on non-agricultural items from EU and European Free Trade Association (EFTA) countries. The simple average tariff for industrial products from the United States and other third countries dropped to 4.4 percent in 2003. Turkey's harmonization of trade and customs regulations with those of the EU and the overall decline in tariff rates benefits third country exporters.

Turkey maintains high tariff rates (25 percent average Most-Favored-Nation rate) on many food and agricultural products to protect domestic producers. Imports of animal products carry the highest tariffs, with ad valorem rates ranging up to 227.5 percent on meat products and edible meat offal. The Turkish government often increases tariffs during the domestic harvest or during times of high stocks. In 2003, the government increased the tariff on corn from 20 to 70 percent. High feed prices have negatively impacted Turkish livestock industries, particularly for beef and poultry. Duties on fruits range from 61 percent to 149 percent. Processed fruits, fruit juices and vegetable tariffs range between 41 and 138 percent. The GOT also levies high duties as well as excise taxes and other domestic charges on imported alcoholic beverages that increase wholesale prices by more than 200 percent.

Import Licenses and Other Restrictions

While import licenses generally are not required for industrial products, products which need after-sales service (e.g., photocopiers, ADP equipment, diesel generators) require licenses. Non-tariff barriers result in costly delays, demurrage charges, and other uncertainties that stifle trade for many agricultural products.

Private traders report that Turkish import policies are often implemented in a nontransparent manner. In addition, gaps in communication between Ankara and regional offices often result in improper implementation of regulations. Turkey is in the process of rewriting its import regulations for agriculture products in order to comply with EU regulations. However, some new regulations have not been fully consistent with those of the EU. For many products, no written standards exist. For example,

despite repeated requests, the GOT failed to provide guidelines for red meat imports. For the past four years, the Ministry of Agriculture and Rural Affairs (MARA), through its quarantine service, stopped issuing import licenses for rice prior to the harvest. In July 2003, the GOT stopped issuing licenses and has not lifted this ban as of December.

The import process for alcoholic beverages is exceedingly complicated, requiring both MARA control certificates and TEKEL (a parastatal company) permits which strictly limit trade and distribution channels and are made available under only limited and unpredictable circumstances. The government is in the process of privatizing the alcohol operations of TEKEL. Recent changes in Turkish law call for a liberalization of the spirits and tobacco market over a five-year period, which should improve the competitive environment.

Turkey applies discriminatory price controls for imported pharmaceuticals, allowing lower mark-ups for imported drugs relative to those produced domestically. U.S. pharmaceuticals companies claim this policy has cost them over USD 250 million since it was last modified in April 2001.

STANDARDS, TESTING, LABELING AND CERTIFICATION

The Turkish government has not consistently notified the WTO of changes in import policies and phytosanitary requirements, and implementation has been arbitrary. Importers have had increasing difficulty in obtaining information on sanitary and phytosanitary certifications. The GOT often requires laboratory testing on items not normally subject to testing by trading partners, often without any scientific basis. Finally, the GOT often requires phytosanitary certification on quality issues that are normally handled on a contractual basis.

The government requires laboratory tests and certification that quality standards are met for the importation of foods, human and veterinary drugs, and medical equipment and appliances intended for use by humans.

GOVERNMENT PROCUREMENT

Turkey is not a signatory of the WTO Government Procurement Agreement. Although its laws require competitive bidding procedures for tenders, U.S. companies sometimes become frustrated over lengthy and often complicated bidding and negotiating processes. Some tenders, especially large projects involving co-production, are frequently opened, closed, revised, and opened again.

In 2003, a new public tender law which establishes an independent board to oversee public tenders, and lowers the minimum bidding threshold at which foreign companies can participate in state tenders, entered into force. However, the law gives a price preference of up to 15 percent for domestic bidders and is not applicable to domestic bidders who form a joint venture with foreign bidders. Amendments to the law in 2003 enlarged the definition of domestic bidder to include corporate entities established under Turkish law, including those established by foreign companies.

Military procurement generally requires an offset provision in tender specifications. The offset guidelines were recently modified to encourage foreign direct investment and technology transfer.

The entry into force of a Bilateral Tax Treaty between the United States and Turkey in 1998 eliminated the application of a 15 percent withholding tax on U.S. bidders for Turkish government contracts.

EXPORT SUBSIDIES

Turkey employs a number of incentives to promote exports, although programs have been scaled back in recent years to comply with EU directives and WTO standards. Historically, wheat and sugar were the main

subsidized commodities. Export subsidies, ranging from 10 to 20 percent of export values, are granted to 16 agricultural or processed agricultural products. The Turkish Eximbank provides exporters with credits, guarantees, and insurance programs. Certain tax credits also are available to exporters.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

Turkey's intellectual property rights regime has improved in recent years, but still presents serious problems. Beginning in 1995, the Turkish Parliament approved a series of patent, trademark and copyright laws in connection with Turkey's customs union with the EU and the WTO Agreement on Trade Related Aspects of Intellectual Property Rights (TRIPS). In recognition of Turkey's progress in the IPR area, USTR removed Turkey from its Special 301 Priority Watch List and placed the country on its Watch List in 2002, where it remained in 2003.

Turkey's 2001 copyright law substantially modernized the legal regime, providing deterrent penalties for copyright infringement. However, it does not prohibit circumvention of technical protection measures, a key feature of the World Intellectual Property Organization (WIPO) "Internet" treaties. In addition, the Turkish courts have failed to render deterrent penalties to pirates as provided in the copyright law. They have instead applied the Turkish Cinema Law, which has much lower penalties. The copyright industries' key demand is for better enforcement. Currently, the police generally do not intervene in pirate production or sales unless the rightholder specifically requests that they do so. U.S. industry estimated losses to piracy at USD 93 million in 2002.

In 1995, new patent, trademark, industrial design, and geographic indicator laws revamped Turkey's foundation for industrial property protection. Turkey also acceded to a number of international conventions, including the Stockholm Act of the Paris Convention, the Patent Cooperation Treaty, and the Strasbourg Agreement. Although the Turkish Patent Institute (TPI) was established in 1994 to support technological progress, protect intellectual property rights and provide public information on intellectual property rights, it is currently understaffed.

In accordance with the 1995 patent law and Turkey's agreement with the EU, patent protection for pharmaceuticals began on January 1, 1999. Turkey has been accepting patent applications since 1996 in compliance with the TRIPS agreement "mailbox" provisions. The patent law does not, however, contain interim protection for pharmaceuticals in the R&D "pipeline."

The key intellectual property concern for research-based pharmaceutical companies is Turkey's lack of data exclusivity protection for confidential test data, which is required by the TRIPS agreement. U.S. industry contends that at least 165 products infringing data exclusivity have been approved or are pending review by the Turkish Health Ministry, and that lack of data exclusivity protection costs U.S. companies some USD 400 million annually in lost sales. Patent holders have also note that the Health Ministry has accepted applications to register generic copies of products which have a valid patent in Turkey.

Trademark holders also contend that there is widespread and often sophisticated counterfeiting of their marks in Turkey. According to one industry association, Turkey is the world's third-largest exporter of counterfeit products.

SERVICES BARRIERS

Telecommunications Services

State-owned Turk Telekom currently provides voice telephony and most value-added and basic telecommunications services. In the WTO negotiations on Basic Telecommunications Services, Turkey made commitments to provide market access and national

treatment for all services at the end of 2005, and permitted value-added telecommunications services to be licensed to the private sector with a 49 percent limit on foreign equity investment. In the interim, Turkey committed to provide national treatment for mobile, paging and private data networks. In 2000, the Turkish government passed a law unilaterally accelerating the opening of the market for basic telephone services to January 1, 2004. A 2001 law provides for liberalization of areas under the Turk Telecom monopoly once the state's share in that company falls below 50 percent. The Turkish government has not yet issued implementing regulations. These laws also created an independent regulatory body - the Telecommunications Regulatory Board - and made licensing criteria publicly available. U.S. firms complain that the licensing process still lacks transparency and that revenue sharing with Turk Telecom is required where competition is permitted. There are three private GSM cellular operators in Turkey, with a fourth license held by Turk Telecom.

The Turkish government plans to announce its strategy for privatizing Turk Telekom in the near future. In November 2003, the Transport and Communications Minister said that the Council of Ministers had agreed on a block sale of a majority stake in Turk Telecom by the end of May 2004, with a possible sale of additional shares to the public after that date. The Minister stated that foreign investors would be eligible to buy a majority stake in the company.

Other Services Barriers

There are restrictions on establishment in financial services, the petroleum sector, broadcasting, aviation and maritime transportation (see Investment Barriers section). A 2003 law on work permits for foreigners repealed earlier legislation defining certain professions and services open only to Turkish citizens. This has significantly broadened the range of occupations in which foreigners can be engaged, but there are still restrictions for doctors, attorneys and several other professions.

INVESTMENT BARRIERS

The U.S.-Turkish Bilateral Investment Treaty (BIT) entered into force in May 1990. Turkey has a liberal investment regime in which foreign investments receive national treatment. Once approved, firms with foreign capital are treated as local companies. However, private sector investment is often hindered, regardless of nationality, by: excessive bureaucracy; political and macroeconomic uncertainty; weaknesses in the judicial system; high tax rates; a weak framework for corporate governance; and frequent, sometimes unclear changes in the legal and regulatory environment.

Almost all areas open to the Turkish private sector are fully open to foreign participation, but establishments in the financial and petroleum sectors require special permission. The equity participation ratio of foreign shareholders is restricted to 20 percent in broadcasting and 49 percent in aviation, value-added telecommunications services, and maritime transportation. Nonetheless, once investors have committed to the Turkish market, they sometimes find the rationale for their initial investments significantly undercut by arbitrary legislative action, such as laws imposing limits on the production corn sweeteners.

The Turkish government accepts binding international arbitration of investment disputes between foreign investors and the state; this principle is enshrined in the U.S.-Turkish BIT. For many years, there was an exception for "concessions" involving private (primarily foreign) investment in public services. In 1999, the Parliament passed a package of amendments to the constitution allowing foreign companies access to international arbitration for concessionary contracts. In 2000, the Turkish government completed implementing legislation for arbitration. In 2001, the Parliament approved a law further expanding the scope of international arbitration in Turkish contracts.

In 2003, Parliament passed legislation which

streamlined the process of establishing a company in Turkey, and which eliminated screening of foreign investors in favor of a notification system, provided national treatment for foreign-owned entities in acquisition of real estate, and abolished of specific minimum capital requirements for foreign investors. The Turkish government passed legislation in February 2001 that will introduce a fully liberalized energy market, under which private firms will develop projects with the approval of an independent regulatory body, but little progress has been made in privatizing power generation and distribution.

ANTICOMPETITIVE PRACTICES

As part of its customs union agreement with the EU, Turkey has pledged to adopt EU standards concerning competition and consumer protection. In 1997, a government "Competition Board" commenced operations, putting into force a 1994 competition law. Government monopolies in a number of areas, particularly alcoholic beverages and telecommunications services, have been scaled back in recent years, but currently remain a barrier to certain U.S. products and services.

Corruption

CORRUPTION IS PERCEIVED TO BE A MAJOR PROBLEM IN TURKEY BY PRIVATE ENTERPRISE AND THE PUBLIC AT LARGE.

Corruption appears to be most problematic in government procurement, with frequent allegations that contracts are awarded on the basis of personal and political relationships of businesspersons and government officials. The judicial system is also perceived to be susceptible to external political and commercial influence to some degree.

U.S. firms have sometimes alleged that corruption, or at a minimum, nontransparent practices, have been a barrier to direct foreign investment. American companies operating in Turkey have complained about contributions to the community solicited, with varying degrees of pressure, by municipal or local authorities.

The Turkish government conducted two significant anti-corruption operations in 2001, one in the energy ministry and the other in the public works ministry. Several individuals were charged with corruption and wrongdoing in government contract tenders. Parliament continues to probe corruption allegations involving senior officials in previous governments, particularly in connection with energy projects. In 2003, after the government intervention in a bank owned by the Uzan group, evidence of corrupt practices at the bank was discovered.

Turkey ratified the OECD antibribery convention, and passed implementing legislation providing that bribes of foreign officials, as well as domestic, are illegal and not tax deductible. In 2003, Turkey ratified the convention on Combatting Bribery of Foreign Public Officials in International Transactions, the Council of Europe's Civil Law on Corruption and the UN Convention against Transnational Organized Crime. The GOT has signed the Council of Europe's Criminal Law on Corruption, but has not ratified it. The Turkish Government signed the UN Convention Against Corruption in Dec 2003.

OTHER BARRIERS

Energy: In 2001, the Turkish Government cancelled 46 contracted power projects based on the build-operate-transfer (BOT) and transfer-of-operating-rights (TOR) models. Turkey's constitutional court ruled in 2002 that the government would have to either honor the contracts or compensate the companies involved. To date, the Turkish government has not commenced negotiations with the companies, one of which has launched an international arbitration case. In 2002, the government required BOT projects already in operation -- which include U.S.-owned companies -- to apply for new licenses from the new Energy Market Regulatory Authority (EMRA), and has pressed them

unilaterally to lower their prices while the license application process is still underway.

Cola tax: Punitive taxation of cola drinks (raised in 2002 to 47.5 percent under Turkey's "Special Consumption Tax") discourages investment by major U.S. cola producers.

Corporate Governance: Weaknesses in the protection of minority shareholder rights and regulatory oversight have left some American companies at a disadvantage in disputes with Turkish partners.

Edelman